FILE COPY

No. 303

IN THE

Supreme Court of the United States

OCTOBER TERM, 1942

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v.

AMERICAN DENTAL CO.

BRIEF IN OPPOSITION TO PETITION FOR CERTIORARI

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May It Please the Court:

It is submitted the writ should be denied because:

(1) The forgiveness of debt was a gift and gifts are expressly excluded from income by the Statute quoted on page 11 of the petition for the writ.

(2) If it was not a gift there was no legal forgiveness of debt.

(3) Even if not a gift, no question is presented on this record whether it was income in 1937 (the only year involved here) because the subsidiary findings of fact compel the conclusion that it was forgiven prior to 1937.

(4) There is no conflict in the decisions of the Circuit Court of Appeals.

ARGUMENT FOR EACH OF THE ABOVE POINTS

Point I.

Unquestionably the forgiveness was without consideration and it is apparently so conceded on page 7 of the petition. (The Board did not find as a fact that the forgiveness was not a gift. It merely stated this in its opinion as a pure conclusion of law from the facts found.)

The Horn book definition of a gift is thus stated in Paul's Law of Federal Income Tax (Vol. 1, sec. 6.05, page 151):

> "A gift has been defined as a voluntary transfer of property by one to another, without any consideration or compensation therefor."

See also *Blair* v. *Rosseter*, 33 F. (2d) 286 (C.C.A. 9th), Such is also the definition in New York where part of the interest was forgiven. See *Gray* v. *Barton*, 55 N. Y. 68, quoted in *Daly*, 3 B.T.A. 1042, 1044. Such is also the definition in Illinois where the balance was forgiven. Berbacker's Estate, 277 Ill. App. 201. The law of the state where the transaction took place supplies the definition. (*Erie Railroad* v. *Tompkins*, 304 U. S. 64). Right in point on the rent item is *Levy* v. *Greenberg*, 261 Ill. App. 541.

In the law of gift donative intent is simply intent to pass title to the donee without consideration and nothing more. Motives and reasons prompting the gift are immaterial. Moore's Estate, 237 Ill. App. 190. No doubt many donors of the thousands of wedding presents given Mar-

shall Goering's bride hoped for some benefit as do many donors of campaign contributions but they are nonetheless gifts.

Income Tax Regulations 45, 62, 65, 69, 74 and 77 all provided as follows:

> "* * * If, however, a creditor merely desires to benefit a debtor and without any consideration therefor cancels the debt, the amount of the debt is a gift from the creditor to the debtor and need not be included in the latter's gross income. * * *" (See Art. 64 of Reg. 77, p. 20.)

The regulations promulgated under the gift tax sections of the Revenue Code have always provided and now provide:

> "Thus, for example, a taxable transfer may be effected by the declaration of a trust, the forgiveness of a debt * * *" (Art. 2, Reg. 79.)

During the time the foregoing income tax regulations were in force Congress many times reenacted the sections of the Revenue Act here involved in identical language, without change thus bringing in operation the rule of legislative approval. *Helvering* v. *Winmill*, 305 U. S. 79, 83. Also this provision of the regulations was quoted and judicially approved in 1936 in *Gibson* v. *Commissioner*, 83 F. (2d) 869 (C.C.A. 3rd), and never disapproved.

The regulation quoted on page 11 of the petition herein does not declare otherwise. None of the examples therein given touch the case at bar. Further, none of them are really cases of forgiveness of debt.

Point II.

If the transaction was not a gift no legal forgiveness of indebtedness took place and hence no question of income arises. There are only two ways known to the law by which legal title to personal property can possibly be transferred in a situation such as here presented. One is by gift. The other is by contract based on a valuable consideration. The last is excluded by the facts found. An examination of all court income tax cases holding no gift took place will disclose they find a transfer based on valuable considerations.

As said in 33 Harvard Law Review at page 691:

> "A gratuitous parol forgiveness of a chose in action is not valid."

In all the cases where the point has arisen the debtors had to sustain it as a gift and failing this it was held no forgiveness took place. *Levy* v. *Greenberg*, 261 Ill. App. 541. *United States* v. *Bostwick*, 94 U. S. 53. See cases collected in Gifts, 24 Am. Jurisprudence, Secs. 11 and 12; also sec. 76, page 770. Also Restatement of Contracts, Sec. 76 (a), pages 83, 85. *Gleason* v. *McDonald*, 103 F. (2d) 837, 838, 839 (C.C.A. 6th).

Point III.

The Subsidiary Findings Show the Forgiveness Took Place Prior to 1937.

The only year here involved is 1937. If the forgiveness took place prior to that year it could not be 1937 income.

The ultimate finding of the Board is that it took place in 1937 but this cannot stand because it is clearly contra-

dicted by the subsidiary and special facts found by the Board.

In *United States* v. *Esnault-Pelterie*, 303 U. S. ....., it is said at page 31:

> "We may, of course, inquire whether the subordinate or circumstantial findings made by the court below necessarily override its ultimate findings of fact and show that the judgment in point of law is not sustainable."

In the same case on an earlier review (229 U. S. at p. 206) it was said:

> "The special findings may not be aided by statements in the conclusions of law or the opinion of the court."

The findings, with regard to the interest, are specific and unquestionably show the interest was forgiven in 1936. They are as follows (R. 39):

> "The petitioner, in November, 1936, owed several creditors for merchandise which they had furnished the petitioner over a period of prior years. The petitioner had been a good customer of these creditors for many years. It had given its interest-bearing notes for the amount which it owed to each creditor. It went to three of these creditors in November, 1936 and asked for cancellation of interest on the notes on the ground that the creditors had made a similar arrangement with their other customers. Three creditors agreed that they would cancel all interest accruing after January 1, 1932."

If the finding may be aided by resort to the uncontradicted evidence on which it is based, the evidence shows the same thing (R. 13 to 15).

The rent was also forgiven prior to 1936.

Point IV.

No Conflict Exists.

The case of *Hadden Co.* v. *Commissioner*, 118 F. (2d) 285, is not in conflict with the case at bar. An examination of the Board's opinion discloses the creditor who forgave the debt was liable for the debtor's obligations and forgave the debt so as not to have to pay them. This release was valuable consideration to the creditor and prevented the forgiveness being a gift. Also it had deducted the items in prior years but had not, as here, offered to pay the tax saved.

Likewise, all the court cases cited in the petition and in the Board's opinion are distinguishable. In *Jane Holding Co.*, 109 F. (2d) 933, there was no forgiveness for the court held, at p. 938, "that it was upon consideration and not gratuitous." *United States* v. *Little War Creek Coal Co.*, 104 F. (2d) 483, involved a compromise contract based on valuable consideration and in *United States* v. *Kirby Lumber Co.*, 284 U. S. 1, there was no forgiveness of anything but a sale and repurchase of bonds on the open market. In *Fitch*, 70 F. (2d) 583, a dividend was distributed to a controlling stockholder.

Petitioner refers to an alleged statement in *Sportwear Hosiery Mills* v. *Commissioner*, 129 F. (2d) 376 (note 29 at page 328) that the case at bar goes beyond the established law. We do not so read it. It quotes the statement that if there was no consideration the intent to give necessarily followed and adds: "If this language means that in every instance where a payment is made without consideration the conclusion necessarily follows that a gift has been made, it goes considerably beyond what was previously thought to be the law."

Of course the statement means no such thing. The court knew if a racketeer or highwayman exacted a payment absence of consideration did not make it a gift.

Cases in accord with the result reached in the case at bar are *Burnet* v. *Campbell Co.*, 50 F. (2d) 487, 488 (App. D. C.) and *Dallas Transfer Co.* v. *Commissioner*, 70 F. (2d) 95, 96 (C.C.A. 5th), which hold forgiveness of indebtedness not taxable income and respondent will seek to sustain the decision on this ground also should the writ be granted. The last cited case indicates the *Hadden* case went on the ground taxpayer had deducted the items in prior years but had not, as here, offered to pay the amount saved.

* * *

A final word as to the tax benefit from deducting the interest and rent in earlier years. Taxation for this reason is on a principle akin to estoppel. That cannot be invoked here, because it was stipulated respondent offered to pay petitioner all the tax it saved by these deductions and respondent rejected the offer (R. 19). Also, even in cases where it could be invoked, it should only serve to make whole the loss and not to impose a penalty, *i.e.*, be confined to the tax benefit.

For the foregoing reasons the writ should be denied.

All of which is respectfully submitted,

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